

## MEMORANDUM OF LEGAL INTERPRETATION

TO: The Members and Personnel of the  
Department of Financial Institutions

FROM: The Policy and Interpretation Committee

RE: Loans In Excess of The Banks Legal Lending Limit

DATE: February 8, 1988

**REVISED: August 8, 1996**

Extensions of credit granted by a bank in excess of the bank's legal lending limit, in accordance with I.C. 28-1-13-1.5 are considered to be serious violations which expose the bank to unnecessary risk and represent a potential for personal liability to each member of the bank's Board of Directors. The question raised to this committee is "when is the lending limit violation corrected." Once an extension of credit has been granted by a bank which is in excess of the bank's legal lending limit the violation, more often than not, becomes a very difficult violation to correct. The only sure way to correct a violation of the bank's legal lending limit is to collect payment of the loan in full. This can be accomplished through payment by the borrower or by payment in full received from another financial institution.

When considering the methods in which a loan in excess of the bank's legal lending limit can be corrected it must be remembered that the violation is the granting of the extension of credit itself, which after the approval and consummation of the extension of credit, has no relationship to the balance currently being carried on the bank's books. As a result, the payment of the excess portion of any loan by the borrower would not correct the violation. The sale of the excess portion of the loan to another financial institution is also not deemed to correct the violation. The violation occurred when the extension of credit was approved and subsequent actions on the part of the borrower or the bank would have no direct bearing on the violation itself. The Board's exposure to personal liability would have to be determined in a court of law.

It must also be recognized that a commitment to purchase, and subsequent sale of the excess portion of a loan, in accordance with the policy regarding loan participations, which was in place at the time of consummation of the original credit would not constitute a lending limit violation.

For the purposes of the Report of Examination, any loan cited in violation of I.C. 28-1-13-1.5 must be followed closely at the time of future examinations. It must also be remembered that any balances charged-off which have not been legally discharged, such as through bankruptcy proceedings, must be included in the total borrowings of any debtor. If the loans remain as obligations to the bank in any manner at the time of the next examination, after being cited as a violation in previous reports, the report must reflect the status of the loan. If the balance of the loan continues to be in excess of the bank's legal lending limit it must again be cited as a violation. The Report of Examination must reflect the current status of the loan if the loan balance has been reduced by the borrower or the excess portion of the loan sold to another financial institution, even if the loans have subsequently been renewed in an amount below the bank's legal lending limit. The violations page of the Report of Examination should indicate the previous violations and the actions taken by the bank that resulted in reducing the principal balance below the bank's legal lending limit. The Report of Examination should further advise the Board of Directors that the activities which resulted in the reduction of the principal balance of the loan in question are not specifically identified as violations in a current report. Any such loans must be continually followed in all future Reports of Examination until such time as compliance with I.C. 28-1-13-1.5 has been achieved even though after the first subsequent examination it will no longer be necessary to detail the violation (loans) in future reports.